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In the Supreme Court of the United States

OCTOBER TERM 1931.

No. 54.

I. J. VAN HUFFEL,
Petitioner,

vs.

TRACE D. HARKELRODE,
Treasurer of Trumbull County, Ohio,
Respondent.

ON WRIT OF CERTIORARI TO THE
COURT OF APPEALS OF TRUMBULL COUNTY, OHIO,
WRIT GRANTED MAY 25, 1931.

SUPPLEMENTAL BRIEF OF RESPONDENT.

G. H. BIRRELL,
Prosecuting Attorney,
Trumbull County, Ohio;

GEO. W. SECREST,
Assistant Prosecuting Attorney,
Trumbull County, Ohio;

GILBERT BETTMAN,
Attorney General,
State of Ohio;

Attorneys for Respondent.

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SUPPLEMENTAL BRIEF OF RESPONDENT.

ARGUMENT.

THE BANKRUPTCY COURT HAD NO AUTHORITY TO REMOVE THE LIEN OF THE STATE OF OHIO FOR TAXES AND THE DECISIONS OF THE SUPREME COURT OF THE STATE OF OHIO, AND OF THE COURT OF APPEALS OF TRUMBULL COUNTY ARE CORRECT.

I.

THE BANKRUPTCY COURT IN THIS CASE NEVER ACQUIRED JURISDICTION OF THE PERSON OF THE RESPONDENT, THE TREASURER OF TRUMBULL COUNTY.

After The Sterling-Knight Company had been adjudicated a bankrupt, a petition was filed with the Referee for an order to marshal liens and sell the real estate belonging

to the bankrupt, in which petition certain mortgage holders and others were named as parties defendant. (Paragraph 3, Finding of Fact, page 20 of Transcript of Record.)

Upon the filing of such petition, the Referee *mailed* notice to the Treasurer of Trumbull County. (Paragraph 4, page 20.)

After receiving, *by mail*, notice of the filing of this application, the Treasurer of Trumbull County *mailed, to the Referee, a statement of the taxes due upon the real estate.* (Paragraph 4, page 22.)

Neither the Treasurer, nor his counsel, the Prosecuting Attorney, was present at any of the proceedings; nor did they have any knowledge of the finding of the court, determining the priority of liens. (Paragraph 5, page 23.)

The *notice of public sale* mailed to the Treasurer, after the order of sale was made by the Referee, *did not state* that the property was to be sold "free and clear of encumbrances." (Paragraph 6, pages 23 and 24.)

From these facts it is clear that the laws governing such proceedings in the bankruptcy court were not complied with.

Notices may be mailed only under the circumstances provided in Sect. 94, Title 11 U. S. C. of the bankruptcy act, which reads as follows:

> "a Creditors shall have at least ten days' notice by mail, to their respective addresses as they appear in the list of creditors of the bankrupt, or as afterwards filed with the papers in the case by the creditors, unless they waive notice in writing, of (1) all examinations of the bankrupt; (2) all hearings upon applications for the confirmation of compositions; (3) all meetings of creditors; (4) all proposed sales of property; (5) the declaration and time of payment of dividends; (6) the filing of the final accounts of the trustee, and the time when and the place where

they will be examined and passed upon; (7) the proposed compromise of any controversy; (8) the proposed dismissal of the proceedings and (9) there shall be thirty days' notice of all applications for the discharge of bankrupts.

b Notice to creditors of the first meeting shall be published at least once and may be published such number of additional times as the court may direct; the last publication shall be at least one week prior to the date fixed for the meeting. Other notices may be published as the court shall direct.

c All notices shall be given by the referee, unless otherwise ordered by the judge."

The only clause under which a notice referring to sales of property is authorized is in paragraph "a(4)", which provides that creditors shall have notice by mail of "all proposed sales of property." As mentioned above, the notice of the sale of property was given in this case, but did not contain any notification that the property was to be sold "free and clear of encumbrances." (Paragraph 6, pages 23 and 24.) There is no provision in this section for the *mailing* of notice respecting the filing of a petition to marshal liens upon real estate, and there is no provision in the bankruptcy act that provides that a notice may be *mailed* for such purposes.

A proceedings to determine the priority of liens is a "plenary" proceedings to which all claimants are entitled to be regularly summoned. The matter of summons has been determined in the case of *Ray v. Norseworthy*, 90 U. S., 128; 23 Law. Ed., 116; in which the court states, in speaking of the attempt to cancel and displace a mortgage without notice:

> "Creditors in such a proceeding must have due opportunity to defend their interests, and must be *properly notified and summoned* to appear for that purpose, or their rights will be unaffected by the proceedings."

This case was later approved in the case of *Factors' and Traders' Insurance Company vs. Murphy,* 111 U. S., 738; 28 Law. Ed., 582, in which the court says:

> "A sale of a bankrupt's property by order of the court, discharged from all liens, does not discharge the lien of one who has a mortgage on the property, but who was not a party to the bankruptcy proceedings."

In re Henderson, 206 Fed., 139, also holds that:

> Mere citation is not sufficient to bar mortgagee.

A general note with reference to cases discussing the difference between "plenary" and "summary" jurisdiction of the bankruptcy court is found in Title 11 United States Code Annotated Section 46, pp. 311-321,—but the above cited cases determine this question.

The requisites of a proper summons are determined by the rules of practice in Courts of Equity, referred to in the general orders in bankruptcy adopted by the Supreme Court of the United States, in conformity with the power conferred by Section 53, Title 11 U. S. C., of the Bankruptcy Act, to-wit:

> "All necessary rules, forms and orders as to procedure, and for carrying this act into force and effect, shall be prescribed and may be amended from time to time by the Supreme Court of the United States."

General order 37 reads as follows:

> "In proceedings in equity, instituted for the purpose of carrying into effect the provisions of the act, or for enforcing the rights and remedies given by it, *the rules of equity practice established by the Supreme Court of the United States shall be followed* as nearly as may be. In proceedings at law, instituted for the same purpose, the practice and procedure in cases at law shall be followed as nearly as may be. But the judge may, by special order in any case, vary the time allowed for return of process, for appearance and

pleading, and for taking testimony and publication, and may otherwise modify the rules for the preparation of any particular case so as to facilitate a speedy hearing."

The rules of practice with respect to notices or summons, for courts of equity of the United States read as follows:

RULE VII.—PROCESS, MESNE AND FINAL.—*The process of subpoena shall constitute the proper mesne process in all suits in equity, in the first instance, to require the defendant to appear and answer the bill;* and, unless otherwise provided in these rules or specially ordered by the court, a writ of attachment, and, if the defendant cannot be found, a writ of sequestration, or a writ of assistance to enforce a delivery of possession, as the case may require, shall be the proper process to issue for the purpose of compelling obedience to any interlocutory or final order or decree of the court.

RULE XII.—ISSUE OF SUBPOENA—TIME FOR ANSWER.—Whenever a bill is filed, and not before, *the clerk shall issue the process of subpoena thereon, as of course, upon the application of the plaintiff,* which shall contain the names of the parties and be returnable into the clerk's office twenty days from the issuing thereof. At the bottom of the subpoena shall be placed a memorandum, that the defendant is required to file his answer or other defense in the clerk's office on or before the twentieth day after service, excluding the day thereof; otherwise the bill may be taken *pro confesso.* Where there are more than one defendant, a writ of subpoena may, at the election of the plaintiff, be sued out separately by each defendant, or a joint subpoena against all the defendants.

RULE XIII.—MANNER OF SERVING SUBPOENA.—*The service of all subpoenas shall be by delivering a copy thereof to the defendant personally,* or *by leaving a copy thereof at the dwelling-house* or usual place of

abode of each defendant, with some adult person who is a member of or resident in the family.

RULE XV. PROCESS, by whom served.—The service of all process, mesne and final, *shall be by the marshal of the district*, or his deputy, or by some other person specially appointed by the court or judge for that purpose, and not otherwise. In the latter case, the person serving the process shall make affidavit thereof.

RULE XXIV.—SIGNATURE OF COUNSEL.—Every bill or other pleading *shall be signed individually by one or more solicitors of record*, and such signatures shall be considered as a certificate by each solicitor that he has read the pleading so signed by him; that upon the instructions laid before him regarding the case there is good ground for the same; that no scandalous matter is inserted in the pleading; and that it is not interposed for delay.

It will be noticed that no subpoena was served upon the Treasurer of Trumbull County, as required by Rule VII, nor in the manner provided by Rules XII, XIII and XV; nor was any pleading subscribed by counsel filed in answer thereto as required by Rule XXIV. Therefore, proper steps were never taken to bring the Treasurer of Trumbull County into court, and no appearance was ever made by the Treasurer in the Bankruptcy Court. Since the Treasurer was not properly notified, and was not a party to this proceedings, the rule set forth in *Rag v. Norseworthy* and *Factors' and Traders' Insurance Company v. Murphy, supra*, applies, and the lien of the State for taxes cannot be affected.

Incidentally, the Treasurer of Trumbull County is a mere ministerial officer of the State of Ohio, and the County is merely a political subdivision of the State for administrative purposes:

Cincinnati vs. Jones, 24 O. C. C. (N. S.) 374 (Motion to certify overruled);

Hunter vs. Commissioners, 10 O. S., 515, p. 520;
State ex rel. vs. O'Brien, 95 O. S., 166.

The State of Ohio cannot be sued except in cases specifically authorized by Statute. There is only one method authorized for attacking taxes in Ohio, to-wit:

> §12075. JURISDICTION OF COURTS OF COMMON PLEAS AND SUPERIOR.—Common Pleas and superior courts may enjoin the illegal levy or collection of taxes and assessments, and entertain actions to recover them back when collected, without regard to the amount thereof, but no recovery shall be had unless the action be brought within one year after the taxes or assessments are collected.

This is not a case which comes within the provisions of that section; and, in a foreclosure suit, the County Treasurer is neither a necessary nor a proper party to the action:

> *Security Trust Co. vs. Root*, 4 O. C. C. (N. S.) 129, approved 72 O. S. 535.

II.

PETITIONER IS NOT AN INNOCENT HOLDER FOR VALUE.

I. J. Van Huffel purchased this property "free and clear of all encumbrances, except taxes for the year 1928," and received a Warranty Deed therefor. At that time the taxes remained unpaid on the tax duplicate of Trumbull County, a public record of which he was bound to take notice:

> *Osterberg vs. Union Trust Co.*, 93 U. S. 424; 23 Law. Ed., 964;
> *In re Harvey*, 10 A. B. R., 567; 122 Fed. 745.

He chose to rely upon the warranty of his grantor in the face of the record of unpaid taxes of Trumbull County.

There were no unencumbered funds in the hands of the Bankruptcy Trustee, from which the taxes might have been paid. The real estate was sold to the first mortgagee, for the sum of $75,000.00—much less than its total claim of $231,000.00. Naturally, the first mortgagee was benefited, and should in equity have paid the taxes. In fact, according to the practice adopted by the Federal Courts, where real estate is of less value than the encumbrances, the Bankruptcy Court should have abandoned this property to the mortgagees, placing on them the burden of paying the taxes and adjusting the rights of other encumbrancers without making an additional expense for the bankrupt estate:

In re Veitch, 101 Fed., 251;
In re Brinker, 128 Fed., 634.

The sale of the mortgaged personal property amounted to $96,527.30, and this amount was paid to the first and second mortgagees on the personal property. Naturally, it would have been inequitable for the court to have taken property or money belonging to these mortgagees for payment of taxes to benefit the mortgagees on the real estate. In fact there was only $2544.46 of unencumbered funds in this estate, and it was necessary to secure contribution from the mortgagees in order to pay the cost of administration, totaling $19,171.46.

In fact, the Court of Appeals, in its original opinion, found that the first mortgagee was allowed to use, and apply the bonds secured by the first mortgage, as a set-off toward the payment of the purchase price, so that no money changed hands in this deal (p. 14 of Record.)

All of these amounts were settled and paid out long before the Treasurer of Trumbull County learned anything of the attempt to avoid payment of the taxes due the State of Ohio. (Paragraph 12, pages 25 and 26, Tran-

script of Record.) When he did learn of the order of the Bankruptcy Trustee, he was too late to take any action in that court because of the provisions of Rule XVII of the District Court of the Northern District of Ohio, to-wit:

> "Every petition for the review of an order made by referee shall be filed with the Referee within ten days from the entry of said order, but the Referee may, on written motion, and upon good cause shown, allow a longer time, not exceeding five days."

Under all these circumstances, and considering that this is a proceeding in equity, in which the Court will look through the form of the proceedings, and consider the basic principle of law applicable thereto, it is clear that the Treasurer of Trumbull County was never in a position to protect himself in this case, except by enforcing and maintaining the lien of the State for taxes, as he has done, against the real estate; whereas, on the other hand, the petitioner purchased the property knowing that taxes existed against the same, and chose to rely upon the warranty of his grantor, which, by this proceeding, expects to enrich itself in the amount of the taxes it should have paid to the State of Ohio.

III.

THE BANKRUPTCY COURT IS WITHOUT JURISDICTION TO SET ASIDE THE LIEN OF THE STATE FOR TAXES.

The general argument of respondent on this subject is set forth in the "Brief of Respondent Opposing the Petition for a Writ of Certiorari" in this case; and, (as we understand the practice in this Court), this Brief need not be repeated or re-written at this time. This general argument is supplemented by the written opinion of the Court of Appeals of Trumbull County, which is copied at pages 13 to 18 of the Transcript of the Record, and

which was approved by the Supreme Court of Ohio. This general argument is further amplified as follows:

A. The petitioner, in his "Brief in Support of the Petition for Writ of Certiorari," admits that the particular question here involved, (to-wit: *Whether an order can be made as against the lien of the State for taxes*), has not been passed upon or decided; and his argument in support of his position is:

> "It would seem, * * *, that, inasmuch as a bankruptcy court must of necessity be authorized to sell property free of all encumbrances * * * there is no reason * * * why that doctrine should alone apply to lien claimants other than the Government, State or County." (Page 28)

The answer to this proposition is indicated by his further statement:

> "There is nothing to be found in the Bankruptcy Act which expressly authorizes the court to sell the property of the bankrupt free and clear of all liens or of any specific lien, or which requires the court to sell the property of the bankrupt subject to all liens, or to any specific lien." (Page 25)

The equity jurisdiction is conferred by Sect. 2, Title 11, U. S. C., of Bankruptcy Act, wherein the courts are invested with such jurisdiction at law or *in equity* as will enable them to:

> (7) "cause the estates of bankrupts to be collected, reduced to money and distributed and determine controversies in relation thereto, except as herein otherwise provided."
>
> (15) "make such orders, issue such process, and enter such judgments in addition to those specifically provided for *as may be necessary for the enforcement of the provisions of this title.*"

The equity powers of the Bankruptcy Courts to *make orders, issue process* and *enter judgments* are only such *as may be necessary* for the enforcement *of the provisions of* the act.

The Bankruptcy Court is a court of limited jurisdiction, (see cases cited pages 6 and 7, Brief of Respondent Opposing Petition for Writ of Certiorari), and if it is a court of limited jurisdiction, i.e., limited by the act of Congress, its authority ought not be extended by judicial construction. In other words, it ought not to be allowed to do under guise of a full fledged court of equity, that which it is unable to do because of lack of authority or jurisdiction granted by Congress. It cannot make itself a court of general equity jurisdiction, when the act creating it limits its powers to those necessary for the enforcement only *of the provisions* of the act itself.

As previously stated, the Bankruptcy Act in all its provisions assumes to protect the taxes due the sovereign states. In fact these taxes are not affected by the bankruptcy proceedings, because not affected by a discharge in bankruptcy, (§35). The Act further provides that the Trustee shall *pay taxes*, and provides that the court can determine only the amount or the legality thereof when that matter is drawn in question. (§104a)

Taxes are not ordinary debts, and have never been treated as such in the Bankruptcy Court:

U. S. vs. Herron, 87 U. S., 251; 22 Law. Ed., 275;
Osterberg vs. Union Trust Co., 93 U. S., 424, 23 Law. Ed., 964;
Merriweather vs. Garrett, 102 U. S., 472; 26 Law. Ed., 197;
In re Brezin, 297 Fed., 300, 3 Syl.

Since the "provisions" of the act give the court authority only to *protect* the State's right to its taxes, under what method of reasoning can it be claimed that "equity" powers are necessary to *destroy* them? There being no power in the Act to discharge the bankrupt, or his property from tax claims, there is no *provision of this title* for *the enforcement* of which such equity jurisdiction *may be necessary.*

We think the proposition is elementary, that jurisdiction must be expressly granted. In the absence of an express grant of such power in the Act, jurisdiction to interfere with the lien of the State for taxes is withheld.

B. Petitioner's Brief is made up of *dicta* from many cases. Some of these refer to the general jurisdiction of the bankruptcy court, and have neither considered nor made mention of the specific application of the bankruptcy law to the question of taxes. Those cases which make reference to taxes, generally fall into the following classifications, which account for the assumption of authority by the Court in these matters:

(1) Where the "amount or legality" of taxes have been questioned:

In re General Film Corporation, 274 Fed. 903;
In re Anderson, 279 Fed., 525;
In re Stavin, 12 Fed. 2nd, 471;
In re Sheinman, 14 Fed. 2nd, 323;
In re Florence Commercial Co., 19 Fed. 2nd, 468.

(2) Where the property was already "*in custodia legis*", and some other court sought to interfere:

Ex Parte Tyler, 149 U. S., 164, 37 Law. Ed. 689;
Murphy vs. John Hoffman Co., 211 U. S., 562; 53 Law. Ed., 327;

Dayton vs. Standard, 241 U. S. 588, 60 Law. Ed., 1190 (Taxes were paid);

Supply Co. vs. Dattle, 44 Fed. 2nd, 159.

(3) Where no lien for taxes is claimed, or is provided by State law:

In re Prince & Waller, 131 Fed., 546, (The state law did not take effect until after the mortgage lien was acquired);

In re Anderson (*supra*);

United States vs. Wood, 290 Fed., 109, (Distinguishes between taxes and other debts due U. S.);

City of Chelsea vs. Dolan, 24 Fed. 2nd, 522;

In re Alamac Operating Corporation, 42 Fed. 2nd, 120.

(4) In many cases the bankruptcy court has assumed to sell the property "free and clear" of encumbrances, and has paid the taxes from the fund created from the sale. Of course, as long as the taxes are paid the State is satisfied, and no question has ever arisen, except between the court and the purchaser as to the application of proceeds held by the court:

In re Kellar, 6 A. B. R., 351; 109 Fed., 131;

In re Reading Hat Mfg. Co., 224 Fed., 786;

Dayton vs. Standard, 241 U. S., 588 (Taxes paid).

While there are statements in some of the above mentioned cases which, when taken alone, appear to question the impregnability of the State's lien for taxes, yet in every case there has existed a fund from which taxes were eventually paid and nowhere has the State been forced to defend its tax lien.

C. On the contrary there are numerous cases which have recognized the power of the State to create tax liens and appear to recognize the inability of the Bankruptcy Court to interfere therewith.

In *Marshall vs. New York*, 254 U. S., 380; 65 Law. Ed., 315, the right of the State to create a tax lien paramount to all other liens is recognized, and the rule adopted, that "the decisions of the highest court of the state as to the existence of the right and its incidents will be accepted by this court as conclusive."

Ex parte Tyler, 149 U. S., 164; 37 Law. Ed., 689, at p. 697:

> "The Courts of the United States have always recognized the importance of leaving the powers of the State in respect to taxation unimpaired. Where the question involved arises under the State Constitution and laws, the decisions of its highest tribunal are accepted as controlling."

(Ohio law and cases are set forth in Respondent's Brief Opposing Writ of Certiorari, pp. 9-11.)

In re Kellar, 6 A. B. R., 351; 109 Fed. 131:

Sale by bankruptcy court "free and clear from all liens" does not affect the statutory lien for taxes.

In re Brinker, 128 Fed., 634:

Sale for less than mortgage,—taxes need not be paid for "the municipalities to whom the taxes are due being secured, in any case, by their lien on the property."

Delahunt vs. Oklahoma Co., 226 Fed., 31:

Lien for taxes attaches to the *res*, without regard to individual ownership. Mortgagor purchasing at sale "free and clear," could not defeat state's lien

Britton vs. Iowa Co., 9 Fed., 2nd, 488:

> Recognizes that a lien created by state law and not provable under Sect. 63 is not affected nor destroyed by bankruptcy proceedings.

From these cases, and from the trend of the opinions in others, it seems that the courts have always recognized the sovereign character of the tax liens of the State:

United States vs. Herron, supra;
Woodyard vs. Sayre, 110 S. E., 689; 24 A. L. R., 1497.

D. As a conclusion, no doubt the Bankruptcy Court in the administration of the funds coming into its control may demand statements of taxes and if the proper tax officers fail to send in such statements, may pay out funds without regard to taxes; the court may determine the amount and validity of any tax claim; the Court may pay taxes from funds in its possession, and thus convey to purchasers at its sales property free and clear of incumbrances;

BUT any order removing or affecting the lien of the State for taxes is ineffectual unless the taxes are actually *paid*.

WHEREFORE, Respondent respectfully submits:

(1) That the Bankruptcy Court never acquired jurisdiction of the person of the Treasurer of Trumbull County, so as to make any order binding either upon him or upon the State of Ohio, which he represented;

(2) That under the circumstances of this case the petitioner is not an innocent purchaser, and is not equitably entitled to relief; and

(3) That the Bankruptcy Court had no jurisdiction to interfere with the lien of the State of Ohio for taxes.

And for these reasons the decisions of the Court of Appeals and the Supreme Court of Ohio should be affirmed.

Respectfully submitted,

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